

RD AN No. 4212 (4279-A, 4287-B and 4280-B)
August 28, 2006

SUBJECT: Business and Industry Guaranteed Loan and Section 9006 Renewable Energy Systems and Energy Efficiency Improvement Guaranteed Loan Program - Transaction Screen Questionnaire and Phase I Environmental Site Assessments

TO: State Directors, Rural Development

ATTN: Business Programs Directors, Rural Development Managers, Community Development Managers, and State Environmental Coordinators

PURPOSE/INTENDED OUTCOME:

The purpose of this Administrative Notice (AN) is to provide guidance on how to evaluate the economic impacts posed by contamination by hazardous substances or petroleum products when determining the liquidation value of real property in the Business and Industry (B&I) Loan Programs. This AN applies to RD Instructions 4279-A, 4287-B, and 4280-B.

COMPARISON WITH PREVIOUS AN:

This AN replaces RD AN No. 4102, dated August 12, 2005, and will expire on August 31, 2006.

IMPLEMENTATION RESPONSIBILITIES:

In liquidation cases, it is the responsibility of the lender to obtain the maximum amount from liquidation. In the liquidation plan submitted to the Rural Business-Cooperative

EXPIRATION DATE:
September 30, 2007

FILE INSTRUCTIONS:
Preceding RD Instructions 4279-A, 4287-B
and 4280-B

Service (RBS), the lender provides an estimate of the current market and the potential liquidation value of the collateral, if the current loan balance, including accrued interest, is less than or equal to \$200,000. An appraisal report by a qualified independent appraiser is required on all collateral securing loans where the current loan balance is more than \$200,000, including accrued interest. The purpose of an appraisal report is to permit the lender and RBS to determine the appropriate liquidation actions. Paragraph VI. A.4., of the Lender's Agreement, Form 4279-4, requires that RBS share the cost of the appraisal report equally with the lender.

In order to formulate a liquidation plan which maximizes recovery, the collateral must be evaluated for the presence of contamination or the release of hazardous substances or petroleum products which may adversely impact the market value of the collateral. An appraisal which does not consider this aspect is incomplete and possibly misleading. Because these environmental evaluations are performed in conjunction with the appraisal process, the cost of these evaluations will also be shared equally between RBS and the lender.

An evaluation of the environmental condition of collateral is made by conducting environmental due diligence in conjunction with the appraisal. Environmental due diligence, in the context of a real estate transaction, is defined as the process of evaluating real estate for the presence of contamination from release of hazardous substances or petroleum products, and determining the effect, if any, the contamination has on the regulatory status or security value of the property. If contamination is present, the cost of environmental restoration activities can be estimated and used to adjust the market value of the collateral. The process of environmental due diligence is designed to reduce the uncertainty regarding the environmental condition of collateral and meet the "appropriate inquiry" and "due care" provisions in the Comprehensive Environmental Response, Compensation, and Liability Act, 42 U.S.C. 9601, *et seq.*

RBS considers the use of the (1) initial investigation using the Transaction Screen Questionnaire (TSQ) and (2) professional evaluation by a Phase I Environmental Site Assessment (ESA) to be acceptable way of conducting environmental due diligence. The TSQ and ESA standards are published by the American Society of Testing and Materials (ASTM E-1528 and E 1527 respectively) as an adequate format for performing due diligence. It is not necessary to complete both steps in performing due diligence if (1) the TSQ concludes an ESA is unnecessary or (2) an ESA is completed without using a TSQ. It is necessary only to complete the level of review required to ascertain and document economic risks posed by contamination.

The ASTM two-step due diligence process is further explained as follows:

The TSQ is the initial level of inquiry which evaluates the environmental condition of collateral and concludes whether or not additional evaluation is necessary. The TSQ is a

series of questions that determine present or past land uses or activities which have the potential for adversely impacting the environmental conditions and market value of collateral. If the results of the TSQ are inconclusive, a Phase I Environmental Site Assessment is needed. (If contamination or hazardous materials are obvious during site visit, the TSQ may be eliminated and a Phase I ESA conducted.

The next level of review, a Phase I ESA, may be necessary to clarify the issues raised by the TSQ. A Phase I ESA is a detailed investigation and evaluation of a property's environmental condition and involves a review of all pertinent records, a site reconnaissance of the property, interviews with current and past owners or operators of the property, and the preparation of a narrative report communicating the findings and conclusions about the environmental condition of the property. The Phase I ESA may indicate a need for further detailed investigation, in the form of a Phase II ESA, to determine the extent of contamination, remediation measures and associated costs. The Agency and the lender, if further investigation is warranted, may share the cost of these additional investigations.

Phase I ESAs are performed by environmental professionals. Such professionals must be trained in the fields of environmental science and engineering and have the experience necessary to perform the ESA, in accordance with the ASTM standards. The environmental professional must develop conclusions regarding the environmental status of a site and, if necessary, develop remedial options and estimate associated costs. This information is then shared with the appraiser so that a more accurate determination of market value can be made. Remediation plans proposed in ESAs need to be cleared with State or local agencies having jurisdiction over site remediation activities.

RBS considers ASTM standards to be an effective way to determine and document the environmental conditions of collateral and reduce the potential effect that an adverse environmental condition will pose to the market value of the property, particularly at the time of liquidation. Lenders should contact the Program Director for further assistance in incorporating environmental due diligence into their liquidation plans. The Program Director will contact the State Environmental Coordinator for advice as needed.

If environmental due diligence is to be conducted other than as stated in this AN, it must first be cleared with RBS in the National Office.

All Section 9006 Renewable Energy Systems and Energy Efficiency Improvement Guaranteed Loans are to be serviced in accordance with RD Instruction 4280-B, section 4280.152.

If you have any questions, please contact the Business and Industry Division Servicing Branch at (202) 690-4103 or the Specialty Lenders Division Servicing Branch at (202) 720-1400.

(Signed by Jackie J. Gleason)

JACKIE J. GLEASON
Acting Administrator
Rural Business-Cooperative Programs